



## 1. Program Information

**Country**  
Tonga

**Practice Area (Lead)**  
Macroeconomics, Trade and Investment

**Programmatic DPF**

**Planned Operations**  
0

**Approved Operations**  
0

**Operation ID**  
P155133

**Operation Name**  
Tonga First Inclusive Growth DPO

**L/C/TF Number(s)**  
IDA-57710,IDA-D1070

**Closing Date (Original)**  
30-Jun-2017

**Total Financing (USD)**  
2,251,502.20

**Bank Approval Date**  
16-Mar-2016

**Closing Date (Actual)**  
30-Jun-2017

	<b>IBRD/IDA (USD)</b>	<b>Co-financing (USD)</b>
Original Commitment	2,000,000.00	0.00
Revised Commitment	2,000,000.00	0.00
Actual	2,251,502.20	0.00

**Country**  
Tonga

**Practice Area (Lead)**  
Macroeconomics, Trade and Investment

**Operation ID**  
P159262

**Operation Name**  
Tonga Second Inclusive Growth DPO ( P159262 )



<b>L/C/TF Number(s)</b> IDA-57710,IDA-60200,IDA-D1070,IDA-D1780,IDA-D3490	<b>Closing Date (Original)</b> 31-Dec-2018	<b>Total Financing (USD)</b> 14775064.03
<b>Bank Approval Date</b> 27-Apr-2017	<b>Closing Date (Actual)</b> 31-Dec-2018	
	<b>IBRD/IDA (USD)</b>	<b>Co-financing (USD)</b>
Original Commitment	15,000,000.00	0.00
Revised Commitment	15,000,000.00	0.00
Actual	14,775,064.03	0.00

**Country**  
Tonga

**Practice Area (Lead)**  
Macroeconomics, Trade and Investment

**Operation ID**  
P159263

**Operation Name**  
Tonga Third Inclusive Growth DPO ( P159263 )

<b>L/C/TF Number(s)</b> IDA-57710,IDA-D1070,IDA-D4580	<b>Closing Date (Original)</b> 30-Sep-2020	<b>Total Financing (USD)</b> 5565640.03
<b>Bank Approval Date</b> 16-May-2019	<b>Closing Date (Actual)</b> 30-Sep-2020	
	<b>IBRD/IDA (USD)</b>	<b>Co-financing (USD)</b>
Original Commitment	5,500,000.00	0.00
Revised Commitment	5,500,000.00	0.00
Actual	5,565,640.03	0.00

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## 2. Program Objectives and Pillars/Policy Areas



## a. Objectives

The Inclusive Growth Development Policy Operation (IGDPO) consisted of a programmatic series of three operations. The original Project Development Objective (PDO) described in the Program Document (PD) for the first operation was to support policy reforms to: *(i) increase fiscal resilience; (ii) support a more inclusive, modern and accountable state; and (iii) support a more dynamic and inclusive economy.* Objectives (ii) and (iii) were adjusted for the third operation in the series, removing the concept “inclusiveness” from the second objective to avoid duplication with the third objective.

For the purposes of this ICRR, the objectives of the series are simplified as follows:

- *Increasing fiscal resilience* by strengthening revenue, debt and expenditure management
- *Supporting government accountability*

*Supporting a more dynamic and inclusive economy* by improving the environment for private sector activity.

## b. Pillars/Policy Areas

The series was structured around three pillars/policy areas. It included 21 prior actions (PAs) spread over the three operations (see Section 3b).

**Pillar 1: *supporting fiscal resilience*** by stronger revenue mobilization, and debt and public service management through revenue and customs legislation; a medium- term debt strategy; and a new public sector remuneration framework.

**Pillar 2: *supporting government accountability and private sector regulation*** by improving compliance with procurement regulations; improving budgetary classifications; introducing more robust systems to pursue audit recommendations; and introducing new regulatory frameworks into selected sectors.

**Pillar 3: *supporting a more dynamic and inclusive economy*** by adopting investor-friendly foreign investment legislation; improving oversight and private participation in public enterprises; and introducing regulation into private sector labor markets.

## c. Comments on Program Cost, Financing and Dates

The three-operation DPO totaled US\$22.5 million equivalent, of which US\$22.6 million equivalent was disbursed. The first operation of the series was approved on March 16, 2016, and the third one closed on September 30, 2020.

DPO 1 was an IDA credit of US\$1.0 million equivalent and a grant of US\$1.0 million equivalent, approved on March 16, 2016, and effective on May 11, 2016. It closed on June 30, 2017, having disbursed US\$2.25 million equivalent.



DPO 2 consisted of two grants and one IDA credit totaling US\$15.0 million, approved on April 27, 2017, and effective on June 15, 2017. It closed on December 31, 2018, having disbursed US\$14.8 million equivalent.

DPO 3 consisted of a grant of US\$5.5 million equivalent, approved on May 16, 2019, and effective on June 18, 2019. It closed on September 30, 2020, having disbursed US\$5.6 million equivalent.

Discrepancies between amounts allocated and amounts disbursed are due to exchange rate fluctuations.

### **3. Relevance of Design**

#### **a. Relevance of Objectives**

The Program Objectives are aligned with government policy and Bank strategy for Tonga and are considered essential elements in building a resilient and inclusive economy while addressing challenges posed by its geography – small islands spread over a large and remote area in the Pacific – which pushes up the cost of economic activity, offers limited scope for growth while the narrow economic base and high reliance on imports leave it vulnerable to economic shocks.

The Bank worked with the government (and development partners –ADB, Australia, New Zealand, EU) to elaborate the key reform actions supported under the Program. They are aligned with the government's national development plan for 2015-2025, and continue themes introduced under previous DPOs, deepening reforms to revenue mobilization and public financial management including reform of state-owned enterprises, and measures to address non-communicable diseases (NCD). They are aligned with the Bank Group strategy as articulated in the Regional Partnership Framework for the Pacific Island Countries 2019-2021. There, the current Program covers three focus areas: strengthening macroeconomic management, protecting incomes and livelihoods by addressing NCDs, and enhancing access to employment opportunities by broadening opportunities for labor mobility.

The macroeconomic policy stance was considered adequate for the GDPO program at the time of GDPO 1 (2016) and for the two subsequent GDPOs. However, with a slow recovery from the 2018 cyclone Gita, and the subsequent twin shocks of COVID-19 and cyclone Harold, the 2020 IMF Article IV consultation assessment of the short- and medium-term outlook in 2021 is of a modest and fragile economy. While proactive and timely actions helped mitigate these external shocks, the economy nevertheless contracted by some 2.5 percent in 2020 and is estimated to have contracted by 3.5 percent in 2021. Tourism and remittance inflows are expected to decline, and reconstruction-related imports, are expected to rise, worsening the current account deficit. Tonga had requested IMF financial assistance under the Rapid Credit Facility

#### **b. Relevance of Prior Actions**

##### **Rationale**



<b>Objective 1 – increasing fiscal resilience</b>		
<b>DPO 1</b>	<b>DPO 2</b>	<b>DPO 3</b>
<p><b>PA1:</b> The Recipient has increased the rate of fuel excise tax by TOP 0.06 per liter (an increase in the rate of 12%) and other excise tax and import duty rates to improve revenue mobilization and strengthen incentives to consume healthy foods (to reduce the incidence of non-communicable diseases, NCDs), as evidenced through the Excise Amendment and the Customs Amendment</p>	<p><b>PA2:</b> The Recipient has increased the rate of fuel excise tax by TOP 0.09 per liter (an increase in the rate of 16%) and other excise tax and import duty rates in order to improve revenue mobilization and strengthen incentives to consume healthy foods, as evidenced through the Excise Amendment and the Customs Amendment</p>	<p><b>PA3:</b> The Recipient’s Cabinet has approved for submission to Parliament a revised Revenue Services Administration Bill that introduces additional avenues for revenue recovery and sets updated and graduated penalties</p>
		<p><b>PA4:</b> The Recipient’s Cabinet has approved for submission to Parliament a new Customs Bill that aligns with international standards (including the Revised Kyoto Convention and World Customs Organization recommended practices) and simplifies customs administration</p>
<p><b>PA5:</b> The Cabinet has approved a new Medium-Term Debt Strategy which has been made public</p>	<p><b>PA6:</b> The Recipient's Cabinet has approved a transparent, target based fiscal anchor system and monitoring framework that supports medium- term fiscal sustainability and a more efficient mix of public spending</p>	
<p><b>PA7:</b> (a) The Recipient’s Remuneration Authority has completed a remuneration review of the public service to ensure equitable, competitive, and fiscally sustainable remuneration and submitted its recommendations to Cabinet; and (b) the Recipient’s Cabinet has reviewed the said recommendations.</p>	<p><b>PA8:</b> The Recipient’s Cabinet has approved and begun to implement a new public service remuneration structure and performance management system to ensure effective public service delivery, adequate pay, and consistency with fiscal sustainability</p>	<p><b>PA9:</b> The Recipient has: (i) realigned the performance management system year; (ii) provided target performance-rating distributions to public institutions; and (iii) clarified the eligibility of public sector employees to receive performance rewards and the application of procedures to manage poor performance, based on a review of its new public service remuneration structure and performance management system</p>
<b>Objective 2: government accountability and private sector regulation</b>		



<p><b>PA10:</b> The Recipient’s Cabinet has approved a revised set of Procurement Regulations, and prepared standard bidding documents and procurement manuals in support of the Regulations</p>	<p><b>PA11:</b> The Recipient has implemented a new procurement tracking database and adopted compliance and performance indicators and associated targets for monitoring system performance, to be publicly disseminated</p>	
<p><b>PA12:</b> A new biannual report of audit recommendations and actions for all ministries and agencies has been prepared, and a new Audit Oversight Committee of Cabinet established and tasked with ensuring timely and thorough follow-up of audit recommendations</p>		<p><b>PA13:</b> The recipient has removed the non-economic items from the economic segment of the Chart of Accounts, which will improve the accuracy and integrity of budget reporting</p>
<p><b>Objective 3: a more dynamic and inclusive economy</b></p>		
<p><b>PA14:</b> The Recipient’s Legislative Assembly has approved a new Communications Commission Act that will establish an independent regulator</p>	<p><b>PA15:</b> Cabinet approved for public consultation a National Energy Bill that includes provisions for multi-sector regulation for all energy subsectors (electricity, gas, petroleum)</p>	
	<p><b>PA16:</b> The Recipient’s Cabinet has approved the Foreign Investment Bill for submission to the Recipient’s parliament, which includes provisions to facilitate foreign investment in the Recipient’s territory</p>	<p><b>PA17:</b> The Recipient’s Cabinet has approved revised foreign investment regulations, which provide clearer and more transparent requirements for foreign investment application</p>
<p><b>PA18:</b> The Recipient’s Cabinet has approved the appointment of shared boards of directors of public enterprises in the information, communications, and technology sector, and the utilities sector to streamline the number of Directors and achieve greater efficiency</p>	<p><b>PA19:</b> The Recipient’s Cabinet has directed the Ministry of Public Enterprises to proceed with a sale of shares in Tonga Cable Ltd</p>	<p><b>PA20:</b> The Recipient’s Cabinet has approved a recommendation that the Ports Authority Tonga adopts a landlord model for Nuku'alofa port</p>
	<p><b>PA21:</b> The Recipient’s cabinet has approved for submission to Parliament the Employment Relations Bill, which will ensure fundamental labor rights are enshrined in domestic law</p>	



## Objective 1 – increasing fiscal resilience

There was a credible results chain linking PAs 1-4 to stronger revenue mobilization and PAs 5-9 to greater fiscal sustainability. Both results chains contributed to enhancing fiscal resilience. Revenue mobilization was strengthened by a better-functioning revenue and customs administration. Fiscal sustainability was strengthened with better medium-term fiscal planning and monitoring, and better management of the public sector wage bill.

**PA1, PA2 – Excise tax and import duty changes to support revenue mobilization and healthy lifestyles.** Tonga has limited options for generating public resources, with excise taxes and import duties the major sources of public revenue, in addition to revenue from remittances and foreign assistance. **PA1** and **PA2** increased in import duties and excise taxes to improve revenue mobilization, while also being used to address a growing fiscal burden from public health interventions to cope with a growing crisis of non-communicable diseases (NCD) by incentivizing healthier food choices through consumer taxes on specific food items. The PAs were expected to result in an average annual increase of 3.2 percentage points in revenue as a proportion of GDP between FY14/16 and FY18/20.

(Relevance PA1 = S; PA2 = S)

**PA3, PA4 – Revenue services administration and customs legislation.** To further strengthen revenue mobilization and bring better control over high cost structures that reduced the competitiveness and consequently fiscal resilience of the economy, a revenue services administration bill (**PA3**) and a customs bill (**PA4**) were introduced. The former (**PA3**) introduced a new public service remuneration structure and performance management system, including new pay scales, a performance management framework and a policy framework to ensure that remuneration and performance management would be consistent with fiscal sustainability (the public sector wage bill covered about 60 percent of domestic revenues). The latter (**PA4**) was to introduce a new customs bill developed to international standards; it was expected to contribute to enhanced customs collection by bringing greater efficiency and lower transactions costs into the system. The two PAs were part of an explicit results chain linking them to improvements in revenue and customs administration and, together with P1 and P2, contributing to improved revenue mobilization.

(Relevance PA3 = S; PA4 = S)

**PA5, PA6 - Medium-term debt strategy and a fiscal anchor system.** Tonga's exposure to external shocks makes careful fiscal management and oversight over public spending crucial. **PA5** introduced a first medium-term debt strategy for a more rigorous vetting of new borrowing, lowering the portfolio risk. It was to be complemented by a transparent, target-based fiscal anchor system and monitoring framework (**PA6**). Both were major factors in strengthening medium term fiscal planning and monitoring, together with PA7-9 contributing to greater fiscal sustainability.

(Relevance PA5 = S; PA6 = S)

**PA7, PA8, PA9 – Improved management and control of the public sector wage bill.** These prior actions were expected to achieve cost savings by removing automatic features of the current system, which contributed to annual automatic pay raises irrespective of performance. **PA7** undertook a remuneration review of the public service to achieve cost savings by removing the automatic features and creating a competitive and more fiscally sustainable remuneration model. **PA8** and **PA9** were to ensure that the new remuneration structure would be implemented with a focus on relevant elements: pay scales, performance



management, consistency of remuneration with fiscal sustainability, and based on consultations with public services. All three PAs would improve management and control of the public sector wage bill and thereby contribute significantly to fiscal sustainability and fiscal resilience.

(Relevance: PA7=S; PA8=S; PA9=S)

## Objective 2 - Supporting a modern and accountable state

This objective supported measures to strengthen accountability and oversight frameworks in the public sector and in private markets. Policy areas included improved procurement systems (PA10, PA11), improved accuracy and integrity in budget reporting (PA12), and improved effectiveness of external audit recommendations (PA13), responding to shortcomings that had been brought to light in PEFA assessments (2010, 2014) and Australia's 2015 assessment of national systems. Reforms under this objective built on previous DPO-supported reforms (in preparation of public accounts, transparency of budget execution information, earlier stages of procurement reform).

**PA10, PA11 – Procurement.** These two PAs addressed accountability for government finances and continued public procurement reform started under a previous DPO series (Economic Reform Support DPO). The reform drew on a 2010 PEFA report that raised issues of low levels of compliance, an absence of usable records for auditing, and a chronic lack of procurement capacity. Improving the procurement process was expected to create more competitive public sector tendering to provide greater value for money. **PA10** introduced a new set of procurement regulations to address the issues identified in the PEFA report, while also removing inconsistencies in earlier regulations, rules and procedures. Complementary measures to build capacity in line ministries to implement the regulations were less effective due to high turnover of staff, according to the ICR (page 20; see also Efficacy Objective 2). **PA11** introduced a new procurement tracking database with a compliance and performance framework to address the lack of capacity to systematically and centrally record and monitor procurement activity. The tracking database established an institutional mechanism that allowed the government to monitor key performance indicators on procurement. Both PAs formed part of a results chain towards better value for money and increased transparency in public spending to improve government accountability. There is reason to be concerned about the government's ability to utilize the instruments provided under PA10 and PA11 due to human resource capacity constraints (Relevance: PA10 = S; PA11 = S)

**PA12 – Budget reporting.** The 2010 and 2014 PEFA assessments noted serious shortcomings in the follow-up to audits. **PA12** introduced procedures that were to ensure follow-up: a bi-annual report on audit recommendations and follow-up actions; and establishment of a Cabinet-level audit oversight committee to monitor that recommendations were being followed. That committee has not met since 2017; instead, an audit committee internal to the Ministry of Finance and chaired by the Minister, meets regularly to consider audit recommendations. While the PA was appropriate, the IEG (page 20) notes that the arrangements were insufficient to meet indicator targets, given the lack of, and need for, capacity at the management and staff levels of the Ministry.

(Relevance: PA12 = S)

**PA13 – External scrutiny.** **PA13** aimed at improving accuracy and integrity in reporting budgetary information and facilitating access to analytical information through the Chart of Accounts (CoA). This, in turn, would allow the classification of expenditures in the budget system to be standardized (including by removing non-economic items from its economic segment). Other, related reforms – redesigning the CoA



and upgrading the economic segment - were to be completed in parallel, based on recommendations under an ongoing Asian Development Bank project.

(Relevance PA13 = S)

### **Objective 3 – Creating a more dynamic and inclusive economy**

The objective, building on a series of earlier DPOs supporting business development, focused on creating a more supportive environment for the private sector. It included reforms in: (i) public enterprises management to increase efficiency and lower costs, (ii) the foreign investment regime to make Tonga more attractive to foreign direct investment; and (iii) labor markets by introducing a first-ever labor law for a more inclusive economy.

**PA14, PA15 – ICT and energy sector regulation.** With small markets, little scope for competition, need for regulation and low capacity to regulate, the government seeks public enterprise reform that raises productivity and maintains reasonable cost structures by striking a balance between the separation of public ownership and regulation, and meeting the additional capacity requirements on the public sector of such a separation. This approach is sought in PA14, PA15, and in PA19 and PA20 below. **PA14** included a new communications commission act establishing an independent utilities regulator. This was to help bring about separation between ownership and regulation of firms and mitigate perceived conflicts of interest in the ICT sector. A further PA, **PA15**, was to approve a national energy bill on multi-sector regulation for all energy sub-sectors for public consultation. It was to bring together regulation of the energy sector under one entity for better-informed decisions, while also helping to clarify regulatory responsibilities in other areas.

(Relevance: PA14 = S; PA15 = S)

**PA16 – Labor conditions.** This PA included the submission to parliament of Tonga’s first employment relations bill, focusing on introducing basic labor protection (right to leave, non-discrimination, fair dismissal, etc.) and reducing gender disparities. It was drawn up with the help of the ILO. The law had a particular resonance in an environment where workers had little bargaining power due to low numbers of employers and low levels of skills and education. Tonga did have provisions under the Public Service Act that established rights for civil servants, but private sector workers were not covered. Since Tonga at the time lacked any form of labor regulation for the private sector, the PA was relevant in securing assurances around basic working conditions

(Relevance: PA16 = S)

**PA17, PA18 – The foreign investment regime.** Low foreign investment (at 3 percent of GDP) is a constraint on growth and job creation in a country that is highly dependent on foreign investment. **PA17** was to lay the groundwork for a foreign investment bill for submission to parliament with the aim of facilitating foreign investments into Tonga – seen as a critical catalyst for private sector development in the country. Such investments have so far been modest, reflecting an overly burdensome and complex legislation that has kept capital inflows at a modest level. The bill includes several key changes rationalizing restrictions on investment and cutting red tape: specifying the definition of foreign investment; clarifying reserved and restricted lists; and providing better guidelines on screening investment applications. In **PA18**, foreign investment regulations were to be subsequently adjusted to provide clearer requirements for foreign investors.



(Relevance: PA17 = S; PA18 = S)

**PA19, PA20, PA21 – Public enterprises.** The ongoing public enterprise (PE) reform aims at full or partial privatization where that is a viable alternative and in the public interest; and at better governance where public ownership is maintained. Such initiatives were expected to improve PE performance through more dynamic management, more rigorous cost containment, privatization, and/or public private partnerships. Ultimately, they were expected to result in a more dynamic business environment. **PA19** aimed at strengthening the management structures of public enterprises in key sectors, seeking greater efficiency and, plausibly, improved PE performance. The initiative introduced joint public-private boards of directors for PEs to address management capacity constraints in the public sector and thereby increase the professionalism of PE management. (There are altogether 15 PEs in Tonga.) **PA20** started a process of separating ownership from regulation with the sale of a minority share of state-owned Tonga Cable to a private sector telecommunications operator in Tonga. This was expected to facilitate the expansion of the telecommunications network throughout the archipelago by attracting new investors. **PA21** involved the adoption of a landlord model for Nuku'alofa port, the main port for Tonga, with service provision entrusted to a private operator (a model that internationally has demonstrated efficiency gains).

Relevance: PA19 = S; PA20 = S; PA21 = S

## Rating

Satisfactory

## 4. Relevance of Results Indicators

### Rationale

**Table 2. Results Indicator, noting associated PAs, baselines/targets, and status**

Results indicator (RI)	Associated PA	RI relevance	Baseline	Target	Actual	Actual Change in RI relative to Targeted change	RI efficacy rating
<b>Objective 1: Fiscal resilience</b>							
RI1(revised): Domestic revenue as share of GDP	PA1 – PA4	MS	21.8% (average FY14-16)	>25% (average FY18-20)	24.2% (average FY18-20)	75%	S
RI2: external borrowing above 35% of GDP which is concessional	PA5	S	100% (FY13-15)	100% (FY16-20)	100%	Targeted change	High



RI3: Ensure that annual budget estimates are consistent with medium term fiscal anchors in budget document	PA6	S	None indicated	Consistency with m-t anchors	Annual budget estimates were consistent w fiscal anchors	100%	High
RI4: Public wage bill as a proportion of domestic revenue	PA8	S	62% (average of FY14-16)	53% or less (ave. FY18-20)	50.1% (ave FY18-20)	132%	S
RI5: Annual moderated performance process completed and ratings used in determining public sector wages	PA7, PA8, PA9	S	No baseline	Yes	New remuneration framework	Achieved	High
<b>Objective 2: Government accountability</b>							
RI6: Proportion of contracts above the small purchases threshold that are subject to open competition	PA10, PA11	MS	35% (FY14)	At least 50% (FY20)	28% (FY20)	-47% (decline)	N
RI7: New economic segment is used in budget systems	PA12	S	Old segment used (FY17)	New segment used (FY20)	New segment completed and used (FY20)	Targeted change achieved	High
RI8 amended under DPO3: Proportion of public accounts audit recommendations noted as "outstanding" in the following year's audit report	PA13	MS	60% (FY17)	40% (FY19,20)	22 issues from previous audit outstanding, 8 resolved in FY19	-65% (increase in proportion outstanding)	N
<b>Objective 3: A more dynamic and inclusive economy</b>							
RI9 amended under DPO3: Regulators for the communication and energy sectors established and operational	PA14, PA15	S	No baseline	Regulators operational for both sectors (FY20)	Communications regulators exist but dependent on Ministry, no energy sector regulators	0 (neither met)	N



RI10 amended under DPO3: Number of basic labor rights (including equal pay for equal work, gender non-discrimination and right to maternity leave) enshrined in domestic legislation	PA16	MS	None of 7 targeted rights in place in 2015	6 in new legislation	Passed by parliament, Not approved by King	Target not fully met	Modest
RI11: Vetted applications from foreign investors	PA17 PA18	MS	21 applications (FY15)	30 applications	27 (FY20)	67% met	Substantial
RI12 amended: Number of public enterprises that have been reformed since 2015	PA19 PA20 PA21	MU	None	At least two	Tonga Cable completed; Ports authority to be completed in FY22	50% met	Modest

**Fiscal resilience**

**RI1 to RI5.** The five results indicators all aimed at measuring PA contributions to building fiscal resilience, either through increased revenue mobilization or through better fiscal management.

**RI1** initially measured the impact of adjustments in excise taxes and import duty rates on the economy; later revised to measure changes in the share of “domestic revenue” in GDP following two hurricanes and the onset of COVID 19. The latter version, while relevant to the extent it included the effects of excise taxes and import duties, was broader in scope and likely to register the effects of a wider selection of revenue sources. Therefore, RI1 only partly measures the impact of the PAs.

**Relevance: MS**

**RI2** and **RI3** related to strengthening medium term fiscal planning and monitoring: RI2 monitored the impact of PA2 (the introduction of a debt strategy) on concessional borrowing as a share of external borrowing; while RI3 (medium term fiscal anchor and monitoring framework for addressing eventual shocks) related to key debt, revenue, and wage bill targets, capturing the impact of PA5, PA8 and PA9, as well as their objectives. Both RIs were relevant and measurable.

**Relevance RI2: S; RI3: S**

**RI4** and **RI5** relate to improving the management and control of a growing and increasingly unaffordable wage bill – the former RI supporting a systematic program of reform of the public service remuneration structure that is likely to contain public wage increases; and the latter introducing a new remuneration framework for



equitable and performance-related pay. Both are well-defined and directly capture the impact of and progress towards the PAs. (PA7, PA8, PA9)

**Relevance: RI4 = S; RI5 = S**

## **2. Government Accountability**

**RI6** measured an increase in the use of competitive tender mechanisms for procurement above the small tender threshold as an indicator of the effect of revised procurement regulations introduced under PA10; and monitored a new procurement tracking data base (PA11)

**Relevance: RI6 = MS**

**RI7** confirmed the use of the new economic segment of the CoA in budget reporting, introducing increased accuracy in standard economic classifications in the government's budget system and in line with PA12. This consolidated all of the government's public financial management reporting requirements.

**Relevance: RI7 = S**

**RI8** measured improvements in the external scrutiny and timeliness of actions to address audit requirements as determined by outstanding audit recommendations (PA13).

**Relevance: RI8 = MS**

## **3. A more dynamic and inclusive economy**

**RI9** was originally to target effectiveness in regulation, measured in terms of regulatory monitoring reports being prepared, supporting PA14 that established an independent regulator. The indicator was subsequently revised for DPO3 to specifically recognize the establishment of communications regulators and the introduction of energy regulators (PA15)

**Relevance: RI9: S**

**RI10** originally measured the number of basic labor rights introduced into in domestic legislation as a result of PA16, including seven basic rights: paid annual leave; notice period for redundancy; severance; equal pay for equal work; gender non-discrimination; maternity leave; paid sick leave. The indicator is relevant as it measures progress towards achieving basic labor rights and their inclusion in domestic legislation

**Relevance: RI10: MS**

**RI11:** The results indicator targets an increase in interest from foreign investors, as measured by the number of vetted applications. In doing so, it provides an indicator of the effectiveness of PA18, introducing revised foreign investment regulations. As an indicator, it is relevant and measurable, albeit also influenced by external factors.

**Relevance: RI11 = MS**

**RI12:** The results indicator for PAs 19, 20, and 21 targets the number of public enterprises that have been reformed in the direction of rationalizing scarce local PE management capacity and increasing private participation in PEs. The indicator was relevant in allowing this monitoring, which measured the diversification of



PEs and the introduction of private interests into the Tongan business community. It was not, however, clear about the reforms that were being undertaken (for instance, restructuring, privatization, and so forth); nor was it designed to adequately capture the likely impact of the PAs on the performance of the involved PEs.

**Relevance: RI12 = MU**

## Rating

Moderately Satisfactory

## 5. Achievement of Objectives (Efficacy)

### OBJECTIVE 1

#### Objective

Improve fiscal resilience

Supported by PAs 1 to 6 and PAs 7 to 9. Progress measured by RIs 1 to 5.

#### Rationale

Fiscal resilience was supported by measures that contributed to stronger revenue mobilization and greater fiscal sustainability. The increase in excise taxes and import duty rates was partly achieved, with positive effects on tax collection and consumption of health damaging products. A revised revenue services administration bill introduced additional sources of revenue, as did a new Customs bill set to international standards, and a simplified customs administration. Positive effects/trends were negatively impacted by external shocks (weather, COVID 19). Still, the ICR indicates a rise in domestic revenues from an average of 21.5 percent of GDP over FY14-16 to 24.2 percent over FY18-20, albeit below the target of 25 percent of GDP set for FY18-20.

Fiscal sustainability was reinforced through stronger medium-term fiscal planning and monitoring, and better management and control over the public sector wage bill. A new medium term debt strategy was approved, as was a target-based fiscal anchor system and monitoring framework – both strengthening medium-term fiscal planning and monitoring. There were two targets – one to maintain concessional borrowing above 35 percent of total external borrowing, the indicator was relevant, measurable, and achieved. A second indicator sought consistency between annual budget estimates and medium-term fiscal anchors over the FY18-20 period. Annual budget estimates for the period were consistent with medium-term fiscal anchors.

In summary, the achievements of four out of five RIs was high, and one – RI1 – was substantial.

Outcomes per results indicator:



RI1 (domestic revenue as a proportion of GDP) increased from a baseline of 21.8 percent on average over FY14-FY16 to 24.2 percent for FY18-FY20, compared to a target of over 25 percent. Thus, the achievement of this RI was substantial.

RI2 (concessional borrowing above 35 percent of GDP) remained at a baseline of 100 percent. The achievement of this RI was high. RI3 (consistency between annual budget estimates and medium-term fiscal anchors); annual budget estimates were consistent with medium-term fiscal anchors. The achievement of this RI was high.

RI4 (public wage bill as a proportion of domestic revenue) declined from a baseline of 57 percent in FY14 to an average of 50.1 percent for FY18-20, surpassing the target of 53 percent or lower. The achievement of this RI was high.

RI5 (annual moderated performance process completed and ratings used in determining public sector wages) – new remuneration framework was applied. The achievement of this RI was high.

Thus, with all RI targets rated either substantial or high, efficacy at the Objective level is rated **satisfactory**.

## Rating

Satisfactory

## OBJECTIVE 2

### Objective

Improve government accountability

Supported by PAs 10, 11 and 13. Progress measured by RIs 6 to 8, of which, the achievements of 2 of 3 RIs were negligible, and one was high.

### Rationale

Improvements in government accountability focused on procurement, budget reporting and audit oversight. All three aimed at addressing weaknesses in the control and accountability of public funds and were expected to increase value for money in public financial management. A revised set of procurement regulations with standard bidding documents and procurement manuals was prepared, as well as a new procurement tracking database. Both were operational. The results, however, fell short of intentions as measured by the results indicator, RI6, which measured increases in the share of contracts subject to open competition. The proportion of such contracts reached only 28 percent in 2020 compared to a baseline of 35 percent in 2014 and a target of 50 percent in 2020. The shortfall reflects a lack of capacity in line ministries to fully implement procurement regulations, as well as a challenging regulatory design with several different levels of rigor for different types of contracts. Thus, the achievement rating of RI 6 was negligible.

A new relevant and measurable economic segment was introduced (RI7), following up on PA12 and improving the accuracy of budget reporting. The achievement rating of RI 7 was high.



External scrutiny and timeliness in addressing public accounts' external audit recommendations (RI 8) (a measure of the effectiveness of audit oversight) did not meet its target of 40 percent of audit matters raised in the previous year still outstanding the following year, with some 70 percent still outstanding in FY19 against a baseline of 85 percent (115 of 136 reports not scrutinized). The achievement of RI 8 was negligible.

With achievement of two out of three RI targets rated negligible, efficacy for this Objective is rated **moderately unsatisfactory**.

## Rating

Moderately Unsatisfactory

## OBJECTIVE 3

### Objective

A more dynamic and inclusive economy

Supported by PAs 6, 10, 14-15, 17-18, 21. Progress measured by RIs 9 to 12.

### Rationale

The objective was to be pursued by seeking improved regulation of markets with little or no competition. Here, the relevant and measurable results indicator (RI 9) targeted effective regulation in the communications and energy sectors, included as prior actions (PA14 and PA15), that is, regulators in the two sectors established and operational. That has not been achieved, as appropriate funds were not allocated in the budget (ICR, para. 45); moreover, the relevant national energy bill had not been submitted to parliament at series' closing. Thus, the achievement of RI 9 was negligible.

Employment relations legislation codifying basic labor rights has been passed by parliament and awaits the King's final approval (RI10). That has not yet occurred, as government is concerned that the legislation may be too onerous for employers at this time (given the recent climatic and environmental shocks). The achievement of this RI was modest.

The series supported a foreign investment bill aimed at facilitating foreign investment in Tonga. However, the outcome – number of vetted applications, and perhaps more importantly, the number of approved applications (RI 11) – appeared to be strongly influenced by external factors (climate, etc.) creating variability from one year to the next rather than showing a trend or indicating that the legislation has the desired effect. The target – vetting 30 applicants from a baseline of 21 – was substantially achieved with 27 vetted in FY20. The achievement of this RI was substantial.

To improve governance and operational efficiency of PEs in an environment with a limited pool of suitable candidates (RI 12), reform focused on selected sectors (ICT and utilities) and involved the appointment of shared boards of directors serving multiple PEs in similar fields. The two shared boards will span utilities, covering Tonga Power Limited, Tonga Water Board and Waste Authority Limited; and ICT covering Tonga Broadcasting Corporation, Tonga Communications Corporation, Tonga Post and Fast Print Ltd. Initially, RI12 aimed at reforming at least four PEs, which was later reduced to two. Finally, only one was completed under the operation, with the second one delayed due to external circumstances but is expected to be completed in



2022. The timetable for this item may have been too ambitious as the target was downsized from four PEs to two during implementation. Thus, the achievement of this RI was modest.

In summary, the progress of the establishment of independent regulators for the communications and energy sectors (RI 9) was negligible; basic labor rights have been codified (RI 10), but are not yet official, therefore progress was modest (RI10); the progress for vetting of foreign investment applications (RI 11) was deemed substantial, albeit strongly influenced by external factors; and there was modest progress in the number of reformed public enterprises (RI 12), targeted at at least four, is currently at one.

With at least half of RI targets rated modest or better, efficacy at the Objective level is rated **moderately satisfactory**.

### Rating

Moderately Satisfactory

## Overall Achievement of Objectives (Efficacy)

### Rationale

The overall efficacy rating draws on the efficacy rating for each Objective, in this case satisfactory, moderately unsatisfactory and moderately satisfactory. Overall efficacy is **moderately satisfactory**.

### Overall Efficacy Rating

Moderately Satisfactory

## 6. Outcome

### Rationale

With the relevance of prior actions rated satisfactory and efficacy rated moderately satisfactory, the operation's outcome is rated moderately satisfactory.

### a. Rating

Moderately Satisfactory



## 7. Risk to Development Outcome

The sustainability of the series' development outcomes is likely to face a number of risks, including natural hazards, macroeconomic risks, limited implementation capacity, and fluctuating political priorities. While efficiencies introduced under the series – continuous dialogue, technical assistance, selectivity in policy choices – are likely to mitigate the impact of those risks, they are likely to continue to influence implementation of each of the series' objectives.

*Fiscal resilience* will continue to face challenges in revenue mobilization and, more generally, in fiscal management: vulnerability to frequent natural disasters and external macroeconomic developments will divert scarce human and financial resources from longer-term reforms to immediate priorities, testing the resilience of more effective tax collection and revenue management. *Stronger government accountability* is still a work in progress, and recent political developments in Tonga have introduced a measure of unpredictability into decision-making at the highest levels that may result in a slower reform process than was originally anticipated, and one that may also deviate from the model introduced under this series. Efforts towards creating a more *dynamic economy* are also still underway: opening markets to competition by regulatory means and by facilitating foreign direct investment have so far only been partially successful, as has been the case with employment legislation. Again, the mixed record of progress reflects political uncertainties in the archipelago. Influencing successful follow-up on all three objectives is Very limited institutional capacity – a small number of civil servants with the necessary qualifications or experience to implement reforms, and often stretched thin among several responsibilities – is also likely to limit implementation of reforms, even when scarce capacity is being buoyed by Bank advice.

## 8. Assessment of Bank Performance

### a. Bank Performance – Design

#### Rationale

The operation was strategically relevant and aligned with government and Bank priorities (see Section 3a). It continued the process of public sector reform that had begun under two earlier DPOs to build resilience against external shocks to the economy through domestic revenue mobilization, while also introducing policy reforms in public financial management and creating an enabling environment for private sector development. Program design drew on the experience under those DPOs, as well as on analytical work by the Bank and IMF, and PEFA assessments in Tonga. That experience underlay the introduction of several features, among them the evidence base for a new fiscal strategy, the remuneration framework, and the performance management system. It also allowed the anticipation of risks such as scarce human and financial resources and political volatility, resulting in PAs that for the most part were directly linked to either outputs or outcomes related to the PDOs. Sometimes, however, they would not be sufficient to reach targeted results (for instance, the establishment of the procurement, audit, and energy regulator, or the underestimation of capacity constraints that especially made itself felt in applying new procurement standards – Efficacy, Objective 2). Program design also drew on a Joint Policy Reform Matrix of priority reform actions developed by the government together with five development partners under World Bank leadership, and including ADB, Australia, New Zealand and the



European Union – a Matrix against which the partners provide budget support, including the focus areas of the current operation.

## **Rating**

Moderately Satisfactory

### **b. Bank Performance – Implementation**

#### **Rationale**

Existing institutional structures were used to implement and monitor the policy actions that were supported in the operation. The Ministry of Finance assumed overall responsibility for coordinating implementation, monitoring and evaluation of the operation; as well as for reporting progress and coordinating actions among government agencies. The Bank team monitored the indicators for each policy area and played a coordinating role among the development partners to ensure that development partners agreed on the implementation of policy actions under the Program.

Client capacity constraints was a significant factor challenging implementation, as was the apparent reluctance on the part of the client to launch into perceived sensitive reforms, for instance labor relations, which might have required more time beyond series' completion to mature.

## **Rating**

Moderately Satisfactory

### **c. Overall Bank Performance**

#### **Rationale**

Bank performance, while adequate in many areas was challenged by an ambitious agenda that introduced relatively complex reforms into an environment with limited capacity.

### **Overall Bank Performance Rating**

Moderately Satisfactory

## **9. Other Impacts**

### **a. Social and Poverty**



While the ICR makes no quantitative assessment, policy actions supported by the series will have a positive effect on poor and vulnerable households, and women: increased taxes on selected consumer goods (alcohol, tobacco, etc.) will reduce consumption of unhealthy goods; the employment act will improve working conditions; while the restructuring of the ports authority will reduce jobs.

### **b. Environmental**

While the ICR makes no quantitative assessment.

### **c. Gender**

See Section 9a.

### **d. Other**

None identified.

## **10. Quality of ICR**

### **Rationale**

The ICR provides a robust evidence base supporting the analysis in the document although it could have made a stronger linkage between the challenges that the operation's interventions were addressing and the subsequent outcomes; now the emphasis is strongly on "PA will do this..." but less so on articulating what deficiency is being addressed. That said, it summarizes well key achievements. In most instances the discussion is mostly results-oriented, allowing assessment of the results and ratings of the operation. ; in some cases, greater emphasis could have been placed on *outcomes* rather than *outputs* (recognizing that that is not always possible. The text is internally consistent, allowing the linking of the various parts of the series. A deviation from this appears to be the ratings for Efficacy and Outcome, both rated Moderately Unsatisfactory. This is based on the assumption that reforms will take time to be fully realized, and when that is the case, it should be reflected in targets and indicators. This is of course valid for many, if not most, reforms, which take time to mature. In Tonga, this may especially be the situation today following the recent volcanic eruption that is likely to represent a severe setback to the country's development in the short to medium term.

### **a. Rating**

Modest

## **11. Ratings**



Ratings	ICR	IEG	Reason for Disagreement/Comments
Outcome	Moderately Unsatisfactory	Moderately Satisfactory	IEG rated PAs satisfactory reflecting their overall relevance and consistency to objectives sought; and efficacy moderately satisfactory, noting that while objectives often were only partly achieved, the process of change was well underway, or achieved, in all key areas.
Bank Performance	Moderately Satisfactory	Moderately Satisfactory	
Relevance of Results Indicators	---	Moderately Satisfactory	
Quality of ICR	---	Modest	

## 12. Lessons

The lessons are drawn from the ICR.

**Institutional capacity and political support should be continuously monitored.** In a dynamic institutional and political environment, frequent changes in key counterparts and ministers highlight the importance of working with a broad set of stakeholders. In this series, this was addressed by requiring all participating ministries to appoint working level staff to support coordination and continuity, as well as introducing regular meetings with the Cabinet and/or the Finance Minister, to maintain political support for the reform.

**Politically sensitive reforms should be well-grounded in client ownership.** Success in the wage bill management reform was grounded in analysis undertaken by the government (with development partner assistance). The reform process started with a review of remuneration to ensure a common reference base, followed by extensive consultation and awareness raising about performance-based pay, including extensive training to support implementation, and regular consultations and adjustments to improve implementation.

**While PAs may be highly relevant to achieving Program objectives, they need to be consistent with capacity constraints and efforts to build capacity.** This series underlined the importance of having a stable team or being able to adjust the reform program (including triggers) to ensure its continued relevance. That was a particular concern in attempting to improve accountability in government, as Tonga struggled to address capacity constraints in trying to implement new procurement regulations, better budget reporting and audit recommendations.,

## 13. Project Performance Assessment Report (PPAR) Recommended?

No